United States Court of Appeals

for the Second Circuit

APPELLEE'S BRIEF

76-4014

IN THE UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

ALFRED H. TURECAMO and FRANCES H. TURECAMO,

Appellees

v.

COMMISSIONER OF INTERNAL REVENUE,

Appellant

ON APPEAL FROM THE DECISION OF THE

UNITED STATES TAX COURT

BRIEF FOR THE APPELLEES

MICHAEL H. SIMONSON
Attorney for Appellees
350 Park Avenue
New York, New York 10022

B

P/S

IN THE UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

No. 76-4014

ALFRED H. TURECAMO and FRANCES M. TURECAMO,

Appellees,

v.

COMMISSIONER OF INTERNAL REVENUE,

Appellant

ON APPEAL FROM THE DECISION OF THE

UNITED STATES TAX COURT

BRIEF FOR THE APPELLEES

ISSUE PRESENTED FOR REVIEW

Whether hospital expenses covered by hospital insurance under Title XVIII, Part A of the Social Security Act, are to be considered as part of an individual's total "support", within the meaning of Section 152(a) of the Code.*

---

* All references to the "Code" are to the Internal Revenue Code of 1954, as amended.

TABLE OF CONTENTS

CITATIONS

Cases:

EDITOR'S NOTE

Pages ___/___ were missing at time of filming. If, and when obtained, a corrected fiche will be forwarded to you.

STATEMENT OF THE CASE

Nature of the Case

This appeal presents but a single issue: whether for purposes of the support test of Section 152(a), hospital expenses covered by Part A of Title XVIII of the Social Security Act, as amended, should be treated any differently than expenses paid under Part B of the same title* and expenses paid by private medical or hospital insurance, which are not counted as an element of support. The Tax Court correctly decided that in determining the actual support of an individual for this purpose, there is no valid basis for distinguishing between Part A Hospital Insurance, on the one hand, and Part B Supplementary Medical Insurance or private hospital insurance, on the other. In his appeal, the Commissioner disputes the Tax Court's holding and argues that Part A Hospital Insurance should be treated like Federal Old-Age Survivors and Disability Insurance benefits ("OASDI") payable under Title II of the Social Security Act,

---

* Hereafter, references to "Part A" and "Part B" will be to Tit. XVIII of the Social Security Act, as amended, 42 U.S.C. sec. 1395, which was added to the Social Security Act by P.L. 89-97 (1965), 79 Stat. 286; "Part A, Hospital Insurance Benefits for Aged and Disabled" will sometimes be abbreviated as "Part A Hospital Insurance"; and "Part B, Supplementary Medical Insurance Benefits for Aged and Disabled" will sometimes be abbreviated as "Part B Supplementary Medical Insurance".

as amended, and similar Government payments (Br. 25)* -- which he mistakenly asserts are uniformly treated as part of the recipient's support.

Statement of Facts

The material facts, as found by the Tax Court (R. 54-57) are not disputed. The Taxpayers, Alfred and Frances Turecamo, are the son-in-law and daughter of Frances Kavanaugh, who was 81 years old during 1970. During that year, Mrs. Kavanaugh made her home with the Taxpayers. On August 5, 1970, Mrs. Kavanaugh was admitted to the Long Island Jewish Hospital in New Hyde Park, New York. She was discharged from the hospital on October 9, 1970, returned to the Taxpayers' home and resided with them until her death in December, 1970.

The Taxpayers provided Mrs. Kavanaugh with 2-1/2 rooms in their home, which she used as her apartment. Through the furnishing of the apartment, food, clothing and occasional entertainment, the Taxpayers contributed about $4,000 toward her support in 1970. (R. 55).

During Mrs. Kavanaugh's stay in the hospital, her total hospital charges amounted to $11,095.75. Of that total, $10,434.75 was covered by Part A Hospital Insurance. The Taxpayers paid the balance of her hospital charges, together

---

* All references to "Br." are to the Brief for the Appellant. References to "R." are to the Record in this proceeding.

with the costs of nursing care required when Mrs. Kavanaugh was at home. In all, the Taxpayers paid $3,531 for her hospital and nursing care during 1970.

Although Mrs. Kavanaugh received $1,140 in social security benefits during 1970, she applied those funds to other items of her support as she saw fit. She did not reimburse the Taxpayers for expenses paid on her behalf.

On their joint 1970 Federal income tax return, the Taxpayers claimed Mrs. Kavanaugh as a dependent. On that assumption, in computing their medical expense deduction under Section 213 of the Code, they took into account the $3,531 in medical expenses that they had paid on her behalf during 1970.

The Commissioner disallowed the claimed dependency exemption for Mrs. Kavanaugh, together with the medical expense deduction claimed by the Taxpayers, asserting that the Taxpayers had not established that she qualified as a dependent. The disallowance presumably resulted from his conclusion that the $10,434.75 payment of Part A Hospital Insurance constituted an element of her support and should be treated as having been furnished by her. As a consequence, the Taxpayers were deemed not to have provided more than one-half of Mrs. Kavanaugh's support during 1970 and were therefore not entitled to the dependency exemption they had claimed.

Disposition Below

The Tax Court, in a reviewed opinion, three judges concurring and four judges dissenting, upheld the Taxpayers and allowed the additional personal exemption and medical expense deduction which they had claimed. In the majority opinion, written by Judge Scott, the Tax Court recognized that in determining whether a taxpayer has contributed more than one-half of an individual's support, both Part B Supplementary Medical Insurance and private hospital insurance payments are not included in determining the dependent's support. The majority concluded that, in determining the dependency exemption, there is no valid basis for distinguishing those payments from payments of Part A Hospital Insurance. (R. 67.)

The concurring opinion, written by Judge Wilbur, agreed with the majority's finding that Parts A and B are interdependent parts of a single comprehensive health insurance scheme (R. 77) and concluded that even if Part A were viewed independently, it would still amount to a hospital insurance program rather than "social welfare". (R. 81.)

The dissenting opinion, written by Judge Tannenwald, accepted the Commissioner's assertion that Part A medical benefits are comparable to state welfare payments and OASDI benefits and, in accordance with the Commissioner's published rulings, should be considered as an amount contributed by the recipient to his or her own support. (R. 96.)

SUMMARY OF ARGUMENT

Hospital expenses paid with the proceeds of private accident or health insurance are not included in an individual's "support". As the Tax Court properly determined, Part A Hospital Insurance is identical in purpose and effect to private insurance and should be treated in the same way.

The conclusion of the Tax Court is buttressed by a factor not stressed in the Tax Court. By the payment of monthly premiums, those not eligible for Part A Hospital Insurance can voluntarily purchase insurance protection under the same program. In Rev. Rul. 64-223, 1964-2 Cum. Bull. 50, the Commissioner determined that when an individual is covered by private medical insurance, the payment of premiums constitute the support element -- not the hospital expenses that are covered by hospital insurance. The same result must surely apply to those voluntarily purchasing Part A Hospital Insurance by the payment of premiums. It would indeed be absurd to reach a different result with respect to those who obtain coverage under the very same program but who pay "taxes" rather than "premiums".

The exceptional treatment accorded hospital insurance proceeds conforms to the average man's concept of what support is. To provide for extraordinary hospital

expenses, a prudent individual will obtain hospital insurance. To a taxpayer contemplating that individual's support, the only hospital care expenses to be budgeted are the cost of hospital insurance premiums and any hospital costs not covered by insurance.

ARGUMENT

I.

THE TAX COURT CORRECTLY HELD THAT HOSPITAL EXPENSES PAID WITH THE PROCEEDS OF PART A HOSPITAL INSURANCE ARE NOT PART OF AN INDIVIDUAL'S "SUPPORT" FOR THE PURPOSES OF CODE SECTIONS 151 AND 152.

A. INTRODUCTION: IN DETERMINING THE AMOUNT EXPENDED FOR AN INDIVIDUAL'S "SUPPORT", THE PROPER FOCUS IS ON THE NATURE OF THE ITEMS TO WHICH FUNDS ARE APPLIED.

Section 151(e) of the Code provides that a taxpayer may take an additional personal exemption for each "dependent" whose gross income does not exceed specified limits. Under Section 152(a), a dependent is defined as an individual coming within one of the prescribed relationships to the taxpayer who receives over half of his or her support from the taxpayer.

Before determining what part of an individual's support has been furnished by the taxpayer claiming the exemption, it is necessary to compute the total amount spent

to support the claimed dependent during the taxable year. Treasury Regulations § 1.152-1(a)(i) broadly defines support to include ". . . food, shelter, clothing, medical and dental care, education, and the like."

Not all payments made by or on behalf of an individual during the year in question will necessarily have been made to provide his or her "support". For example, in Rev. Rul. 56-399, 1956-2 Cum. Bull. 114, the amount paid for an automobile was determined not to have been applied to support the claimed dependent, even though the transportation costs avoided by its purchase would apparently have represented support payments. Similarly, Federal, state or local income tax payments, Rev. Rul. 58-67, 1958-1 Cum. Bull. 62, funeral expenses, Rev. Rul. 65-307, 1965-2 Cum. Bull. 40, and burial insurance, Eddie L. Carter, 55 T.C. 109 (1970), have all been treated as non-support items, even though the funds in question had clearly been applied on behalf of the person claimed as a dependent.

Having calculated the total amount spent to support the claimed dependent, it is then necessary to determine the source of the funds applied to his or her actual support. If more than one-half of those funds have been provided by a taxpayer, that taxpayer is entitled to the dependency exemption.

B. ALTHOUGH MEDICAL EXPENSES, SUCH AS HOSPITAL COSTS COVERED BY PART A BASIC MEDICARE, ARE ORDINARILY PART OF AN INDIVIDUAL'S SUPPORT, WHEN COVERED BY INSURANCE, THE ELEMENT OF "SUPPORT" IS THE PREMIUMS PAID TO OBTAIN THAT COVERAGE, NOT THE MEDICAL EXPENSES PAID WITH INSURANCE PROCEEDS.

As a general rule, medical expenses paid for the benefit of an individual are to be considered part of his or her support. The Taxpayers agree with the majority opinion below (R. 67) that if the hospital expenses paid in this case with the proceeds of Part A Hospital Insurance had not been covered by insurance, they would have comprised an item of Mrs. Kavanaugh's "support". However, when medical care is covered by insurance, the Commissioner concedes that there is an exception to the general rule of Treasury Regulation § 1.152-1(a)(2)(i).

In Rev. Rul. 64-223, supra, the Commissioner specifically rejected the district court holding in Samples v. United States, 226 F. Supp. 115 (N.D. Ga. 1963), and determined that where an individual is covered by a renewable term policy providing insurance against medical costs, amounts paid by the insurance company under the policy are to be disregarded in determining the individual's support. The same conclusion was reached by the Third Circuit in Mawhinney v. Commissioner, 355 F.2d 462 (1966), aff'g. per

curiam, 43 T.C. 443 (1965). In each instance, it was determined that it was the premiums paid to obtain the insurance coverage, rather than medical costs paid with the proceeds of the policy, that represented the individual's support. The Commissioner has extended the same treatment to Part B Supplementary Medical Insurance proceeds which he concedes are "in the nature of medical insurance proceeds." Rev. Rul. 70-341, 1970-2 Cum. Bull. 31, 32.

This exception to the general rule accords well with the average man's conception of his medical care costs. As pointed out in the concurring opinion of Judge Wilbur (R. 75, n. 1), a prudent individual considers his health costs to be the sum of his health insurance premiums and his unreimbursed payments for medical care. On the other hand, "[viewing large third-party payments (made when the contingency insured against occurs) as support can be viewed as distorting the economic realities."

C. PART A BASIC MEDICARE PAYMENTS SHOULD BE TREATED IN THE SAME MANNER AS PRIVATE HEALTH INSURANCE PROCEEDS IN DETERMINING THE TOTAL SUPPORT OF AN INDIVIDUAL FOR THE PURPOSES OF CODE SECTIONS 151 AND 152.

Hospital expenses paid with the proceeds of Part A Hospital Insurance fall within the exception cared out for expenses covered by private hospital insurance, and, likewise, are not to be considered an element of an individual's support.

This result is mandated by the essential insurance nature of Part A Hospital Insurance. By definition, insurance is "the business of insuring persons or property; coverage by contract whereby one party undertakes to indemnify or guarantee another against loss by a specified contingency or peril." Webster's Seventh New Collegiate Dictionary (7th ed. 1970). The Commissioner's argument that Part A Hospital Insurance is tantamount to a social welfare program (Br. 42-48) is patently absurd* and ignores these basic characteristics of Part A Hospital Insurance:

1. Part A Hospital Insurance is Part of a Comprehensive Public Health Insurance Program

Although proposals for a compulsory health insurance program covering persons of all ages had been made since the early 1900's, Title XVIII of the Social Security Act, commonly called Medicare, was enacted for the specific purpose of providing a coordinated and comprehensive approach to health insurance and medical care for the aged. (H.R. Rep. No. 213, 89th Cong., 1st Sess. 2 (1965).) The Medicare program consists of: "Part A, Hospital Insurance Benefits for Aged and Disabled", a basic plan providing protection against the costs of hospitalization and related care; "Part B, Supplementary

---

* It is as if a casual observer had attempted to classify a young shark by comparing it to a slightly older, more wrinkled shark: if told by the Commissioner that the second specimen was really a dolphin, the observer would look at the Commissioner with great skepticism. But see, Commissioner's Brief, p. 41.

Medical Insurance Benefits for Aged and Disabled", a voluntary supplementary plan covering payments for physician's services and other medical and health services not covered by the basic plan; and Part C, Miscellaneous Provisions", which includes definitions that apply to both Part A and Part B.

Part A Hospital Insurance is available to all persons aged 65 or over who are "entitled" to monthly OASDI cash benefits or to similar payments under the Railroad Retirement System. "Entitlement" simply means that the person (or an eligible dependent) has attained the required age and has the required quarters of coverage. Under a phase-in rule, benefits were also made available to a limited class of persons who reached age 65 without having earned the required quarters of coverage.

To separate the Medicare health insurance system from the cash benefits system of OASDI, Part A insurance is primarily funded by a separate compulsory payroll tax contribution and a parallel contribution imposed on employers. These contributions feed into a separate trust fund. Sections 1401(b), 3101(b) and 3111(b) of the Code. Part B Supplementary Medical Insurance is financed by a combination of voluntary premium payments by those currently being protected and matching contributions from out of general revenues. Social Security Act Secs. 1817, 1839, 1841 (Health Insurance for Aged and Disabled, 42 U.S.C. § 1395i, § 1395r, § 1395t.)*

---

* Hereafter, references to the Social Security Act will be abbreviated by reference to the appropriate Section and followed by a parallel citation to 42 U.S.C.

The legislative purpose of the Medicare program and the constant interplay between Parts A and B, as two components of an integrated public health insurance program, are detailed in the concurring opinion of Judge Wilbur (R. 76-81).

2. Participants Pay for Part A Hospital Insurance

Part A Hospital Insurance is only available to individuals who pay for it, except for those without the requisite social security coverage who were included by Medicare's initial phase-in rules. Those who have not gained entitlement by qualifying for social security coverage and by paying the separate payroll tax that finances Part A Basic Medicare, can voluntarily enroll in the program by paying monthly premiums.

3. Part A Basic Medicare is Intended to be a Separately-Funded Self-Supporting Insurance Program

The Part A Hospital Insurance program is separately funded. Contributions are calculated in accordance with actuarial methods that are designed to insure actuarial soundness. Section 1817 (42 U.S.C. § 1395i; see H.R. Rep. No. 213, 89th Cong., 1st Sess. 47-50 (1965)). Because the Part A program is fully-funded

through contributions by covered individuals, in at least one respect it is more closely identifiable with private hospital insurance than is Part B's supplementary coverage, roughly one-half of which is funded out of general revenues.

4. Pooling of Risks

The Part A Hospital Insurance program, like any insurance program, involves a pooling of risks. Because hospital treatment represents the costliest item of health care for the aged, payroll tax financing was selected as the most appropriate means of meeting the contemplated costs of hospital care, without bankrupting the Federal treasury. Instead employees (and their employers) are required to make advance payments to the Part A trust fund during their lower-risk working years. (111 Cong. Rec. 7213-7214 (1964) (remarks of Congressman Mills).)

5. Benefits Under Part A Basic Medicare Are Payable Only Upon Specified Contingencies

As with other insurance programs, Part A Hospital Insurance covers only those contingencies that are spelled out in the legislation. Section 1813 (42 U.S.C. § 1395d).

6. The Part A Program is Administered by the Private Insurance Industry

The administration of Part A Basic Medicare

claims has been largely delegated to the private sector. Section 1816 (42 U.S.C. § 1395h).

7. Part A Hospital Insurance is Restricted as to Its Use

Unlike the OASDI benefits and state welfare benefits to which the Commissioner compares them, amounts paid out under Part A Basic Medicare are not made generally available to the recipient. They can only be applied against covered expenses.

8. No Means Test

Part A Hospital Insurance was intentionally designed to avoid any resemblance to a welfare program that provides medical assistance to the elderly.* Part A Hospital Insurance serves a restorative function, not a supportive one. Part A Basic Medicare provides insurance: in consideration for the payment of contributions, covered participants are indemnified against specified risks. An individual provides for his or her health care by insuring against major hospitalization costs that could not comfortably be met with funds available for current use.

---

* At the same time Medicare legislation was enacted, Congress enacted a new and separate title XIX to provide expanded medical assistance to the indigent. Title XIX is solely for the needy and a means test determines eligibility. Section 1902 (42 U.S.C. § 1396). This program is commonly known as Medicaid.

9. Medicare has Essentially Replaced Private Health Insurance for the Elderly

Before the enactment of Medicare, approximately 55 to 60 percent of the elderly were covered by some form of health insurance; about half of those covered were enrolled in Blue Cross-Blue Shield plans. Medicare resulted in a total readjustment in the private health insurance industry. For the most part, smaller insurers have completely dropped insurance coverage for the elderly. Because Medicare provides essentially the same coverage, most major medical policies covering individuals or families terminate coverage upon attainment of age 65. For example, Blue Cross-Blue Shield of New York automatically terminates its coverage when participants qualify for Medicare, a policy permitted under New York State's Insurance Law. (Insurance Title 11, N.Y.C.R.R. § 52.16(c)(8) (1972).)

D. THOSE NOT OTHERWISE ELIGIBLE FOR PART A BASIC MEDICARE CAN VOLUNTARILY ENROLL IN THE PROGRAM BY PAYING PREMIUMS; MEDICAL EXPENSES PAID ON THEIR BEHALF ARE NOT AN ITEM OF SUPPORT, AND IT WOULD BE ILLOGICAL TO REACH A DIFFERENT RESULT IN THE CASE OF ELIGIBLE INDIVIDUALS WHO HAD PAID "TAXES" RATHER THAN "PREMIUMS"

Individuals 65 and over who are not otherwise eligible for Part A Basic Medicare coverage under the regular provisions of the law, can voluntarily enroll in

the program by paying monthly premiums. Section 1818 (42 U.S.C. § 1395i-2.) The premiums, currently $45 per month, are actuarily determined on a basis calculated to cover the total cost of hospital insurance protection for voluntary enrolees. Section 1818(d)(1) (42 U.S.C. § 1395i-2(d); 39 Fed. Reg. 45305 (1974).) To reduce the possibility of excessive utilization of the more costly Part A Hospital Insurance coverage, eligibility for voluntary enrollment in Part A Basic Medicare requires concurrent enrollment for Part B Supplementary Medical Insurance benefits. Section 1818(a)(2) (42 U.S.C. § 1395i-2(a)(2).)

A state agency or any other public or private organization can purchase group Part A Hospital Insurance that covers its retired or active employees when they reach age 65. Group premium payments are made under a contract entered into between the agency or organization and the Secretary, but only where it is determined that such method of premium payments is administratively feasible. Section 1818(e) (42 U.S.C. § 1395i-2(e).)

Even the Commissioner must concede that with respect to those voluntarily enrolled in the Part A Basic Medicare program, either individually or as part of a group, the insurance coverage obtained by paying premiums is no different than private hospital insurance. Under the rationale of Rev. Rul. 64-223, supra, and Mawhinney v.

Commissioner, supra, when an individual has voluntarily enrolled in the Part A program, his or her premium payments will represent the element of support -- not the hospital expenses that are insured under the program. It would truly be incongruous to reach a different result in the case of those, like Mrs. Kavanaugh, who have become eligible for Part A Hospital Insurance through the payment of payroll taxes, rather than premiums.

E. EVEN IF THE CONGRESSIONAL PURPOSE IN ENACTING PART A BASIC MEDICARE COULD BE DETERMINED, THAT PURPOSE IS IRRELEVANT; REGARDLESS OF MOTIVE, GOVERNMENTAL PAYMENTS COUNT AS SUPPORT ONLY IF ACTUALLY APPLIED TO SUPPORT ITEMS

The Congressional intent in enacting the Medicare legislation in general, and Part A in particular, has no bearing on Section 152(a)'s support test. The Commissioner is apparently intent on showing that Part A Hospital Insurance is not really "insurance" but rather "social insurance" (Br. 25-35), whatever that is, perhaps something more closely resembling "social welfare" (Br. 41) than health insurance. However illuminating, the Commissioner's 23-page analysis of the legislative history of Part A Basic Medicare (Br. 25-48) is irrelevant. His own consistent position, and the principle adopted by the courts, is that Governmental payments are to be considered as support furnished by the recipient

only when actually expended to pay for items of support.* If the recipient banks the proceeds, gives them away, or uses them for any other non-support purpose, then the Commissioner has determined that such payments are to be disregarded for support purposes. I.T. 3723, 1945 Cum. Bull. 122 (Government family allowance); I.T. 3834, 1947-2 Cum. Bull. 29 (benefits derived by a veteran under the Servicemen's Readjustment Act of 1944, 58 Stat. 284); Rev. Rul. 57-344, 1957-2 Cum. Bull. 112 (survivor's insurance benefits under § 202(d) of Title II of the Social Security Act).

The Tax Court applies the same principle. In Eddie L. Carter, supra, the taxpayer claimed his grandmother as a dependent even though the amounts he provided her were less than the old-age assistance payments she received from the State of Texas during the same year. In allowing the exemption, the Tax Court determined that the taxpayer's grandmother had not spent all of the old-age assistance allowance on her support. She had applied enough of that allowance

---

* Although the Commissioner has sometimes called attention to this principle in his brief (Br. 17-18), he has more frequently ignored it and made the misleading suggestion that the Regulations, the rulings or the Commisioner have consistently or uniformly held that all Governmental payments received by, or paid for, the benefit of an individual are to be considered as support furnished by that individual (Br. 8-9, 20-21, 37, 39 and 48). This suggestion is belied by his own holdings in I.T. 3723, I.T. 3834, and Rev. Rul. 57-344, infra.

to non-support items, such as burial insurance and gifts to others, to reduce the portion supplied by the state for her support to an amount less than the support payments made by her grandson.

The rulings and cases make clear that, for purposes of the support test, Governmental payments are not subject to uniform treatment. The relevant question is not the legislative intent behind the Governmental program, but whether the Government-source payments have in fact been applied to support a claimed dependent. Since it is conceded in this case that $10,434.75 of Mrs. Kavanaugh's hospital expenses were paid for by Part A Hospital Insurance, the only point in issue is whether the same treatment accorded expenses paid with the proceeds of both private hospital insurance and Part B Supplementary Medical Insurance, is to be given to expenses covered by Part A Hospital Insurance. As the Tax Court correctly decided, in viewing the dependency support test there is no rational basis for distinguishing Part A Hospital Insurance form Part B Supplementary Medical Insurance and private hospital insurance.

II.

FUNDS THAT ARE MADE AVAILABLE TO AN INDIVIDUAL, WITHOUT RESTRICTION, AND THEN USED TO MEET DAY-TO-DAY LIVING COSTS, HAVE BEEN USED BY THAT INDIVIDUAL FOR HIS OR HER OWN "SUPPORT." BUT FUNDS THAT ARE ONLY RECEIVED IN THE EVENT OF SERIOUS MEDICAL PROBLEMS AND THAT MUST BE USED FOR SPECIFIED HOSPITAL COSTS, IN NO WAY RESEMBLE SUPPORT

Although the definition of support provided in Treasury Regulation § 151.2(a)(i) covers a broad range of expenses, the items specified -- "food, shelter, clothing, medical and dental care, education and the like" -- can all be described as ordinary, day-to-day living expenses. The same characteristic is shared by the other itemized expenses that have been counted as support: baby-sitter costs, William K. Price, 20 CCH Tax Ct. Mem. 886 (1961); church contributions, Rev. Rul. 58-67, 1958-1 Cum. Bull. 62; child care, Thomas Lovitt, 18 T.C. 477 (1952), (Acq.) 1952-2 Cum. Bull. 2; music lessons, Miriam G. Sauer, 12 CCH Tax Ct. Mem. 1377 (1953); dancing and dramatic lessons, Raymond M. McKay, 34 T.C. 1080 (1960); school lunches, Everett J. Tucker, 19 CCH Tax Ct. Mem. 210 (1960); premiums on accident and health insurance, Rev. Rul. 64-223, supra; miscellaneous items, such as haircuts, toilet articles, permanent waves and vitamins, Everett J. Tucker, supra; pet care costs, Raymond M. McKay, supra;

transportation, Ward L. Horitz, 25 CCH Tax Ct. Mem. 1468 (1966); and recreation expenses, George E. Hulse, 25 CCH Tax Ct. Memo 556 (1966).

Major medical and hospital expenses are quite different. To a budget-minded individual, they are difficult to anticipate, both as to timing and to magnitude. Because the cost of hospitalization and medical care can be prodigious, the funds available to the average individual for daily living costs could not begin to meet them. For this reason, the prudent individual will eliminate this concern from his or her expense budget by obtaining medical insurance. Having done so, the budget item becomes the monthly premium payment or, as in this case, the payroll tax payment to provide for hospital insurance.

Moreover, unlike OASDI, state welfare and most other governmental payments, Part A benefits cannot be used to pay an individual's daily living expenses. Funds, the availability of which is triggered by a serious medical incident, the use of which is restricted, and the purpose of which is the restoration of the individual to his or her prior condition, do not resemble support.

In the case at bar, the record clearly shows that the only funds that were at the disposal of Frances Kavanaugh in 1970 consisted of the $1,140 that she received in social

security benefits and used for her own support. These payments, apparently her only outside source of income, hardly made her self-supporting. The Taxpayers took her into their home and provided her with two and a half rooms, furniture and her own telephone. They fed her, bought her clothing and provided for her entertainment. The cost of these items, which the Turecamos might well have anticipated in making out an expense budget, amounted to approximately $4,000.

During the year in question, Mrs. Kavanaugh became seriously ill; she required nursing care and then extensive hospitalization. The Taxpayers expended $3,531 for hospital and nursing care, bringing their actual support of Mrs. Kavanaugh to $7,531. Out of a total of $11,095.75 in hospital charges, the lion's share, $10,434.75, was covered by Part A Hospital Insurance (R. 55-56).

When Mrs. Kavanaugh moved in with her daughter and son-in-law, their clear intention was to "support" her. In anticipating that kind of responsibility, a prudent taxpayer would try to calculate the expenses that would ordinarily have to be met to support the dependent. On that basis, major medical costs and the costs of hospital care will be considered an expense to be met only to the extent not covered by insurance. If the dependent is adequately covered by insurance, then his or her "support" --

in the ordinary sense of the word -- will not include hospital care but only the premiums payable to maintain adequate hospital insurance coverage.

In deciding whether he or she is financially capable of supporting the dependent, the taxpayer will often take into consideration the after-tax cost of providing the anticipated support. This will depend upon two considerations. The first is whether the burden of supporting the dependent will be offset in part by an additional personal exemption; if so, then, in addition, any medical expenses paid by the taxpayer on behalf of the dependent can be taken into account in determining the taxpayer's medical care deduction.

If the Commissioner prevails in his argument, a taxpayer willing to volunteer his home and resources for the support of his relative could never be certain that those tax benefits will be available, even if he or she were willing to shoulder 100% of another's expected support. If extraordinary medical costs were unexpectedly incurred and paid for by Part A Hospital Insurance, the taxpayer would lose the expected tax benefits if those insurance proceeds exceeded the taxpayer's support contributions.

Because private insurance companies will no longer provide health insurance coverage that duplicates the

Medicare coverage available to those eligible for Medicare, the Commissioner's policy would in many cases deprive taxpayers supporting their elderly parents of a dependency exemption, even where the parents are clearly dependent upon their children for support.* Indeed, the result urged by the Commissioner could in many cases provide a disincentive to support and cause a return of the elderly to the country's welfare rolls.

III.

THE FACT THAT TAXES PAID TO FUND PART A HOSPITAL INSURANCE ARE NOT DEDUCTIBLE UNDER CODE SECTION 213, IS IRRELEVANT FOR DETERMINING SUPPORT UNDER SECTIONS 151 AND 152

The Commissioner points proudly to his "extensive analysis" (Br. 21) in Rev. Rul. 70-341, supra, which, with self-styled "persuasive inherent logic and symmetry" (Br. 24), presents a false syllogism. The Commissioner's major premise is that Part A Hospital Insurance payments are "in the nature of disbursements made in furtherance of the social welfare objectives of the Federal Government" (Br. 22). To that major premise he adds a minor

---

* The Commissioner's heavy-handed suggestion that "the basic principles at issue here involve billions of dollars of revenue annually" (Br. 8), is absurd on its face.

one -- that taxes paid to fund Part A Hospital Insurance are not deductible as premiums paid for medical care insurance under Section 213 of the Code (Br. 22).* To complete his syllogism, the Commissioner reaches the irrelevant conclusion that because the taxes funding the Part A program are not deductible as medical expenses, Part A Hospital Insurance benefits received by an individual are to be counted as amounts that the individual has contributed to his or her own support in determining whether another taxpayer might be entitled to claim that individual as a dependent.

The Commissioner's logic is flawed. As the Taxpayers have already indicated in their first argument, his major premises is false. Inevitably, a compulsory health insurance program of this scope will provide widespread social benefits. But Part A Hospital Insurance is nonetheless hospital insurance. Even assuming that Part A of the Medicare program was the brainchild of social welfare advocates, their invention is, in actuality, a comprehensive separately-funded, self-supporting insurance program.

---

* By the juxtaposition of these premises, the Commissioner apparently means to suggest that the non-deductibility of Part A taxes as health insurance premiums somehow depends on the truth of his major premise, that Part A benefits are tantamount to social welfare payments.

Secondly, though taxes contributed by an individual as his or her share of the Part A trust fund are not deductible as medical expenses under Section 213, they should certainly be considered as the payment of a support item. Their payment is the functional equivalent of the payment of Part A premiums by individuals voluntarily enrolling for Part A Hospital Insurance,* the payment of Part B premiums, or the payment of private medical insurance premiums. All such premium payments are support items, and the payroll taxes withheld to obtain the same or similar insurance coverage should be treated no differently.

Finally, Congress' failure to allow a medical expense deduction for taxes paid to fund Part A Hospital Insurance cannot be taken as an indication that it considered that program to be a welfare program. As the Commissioner points out in his brief (Br. 43), Congress can make any payment deductible or not as Congress sees fit and, as noted in Judge Wilbur's concurring opinion (R. 170, n.21), to permit a medical expense deduction for such taxes would result in some unrelated administrative problems.

---

* Although the Commissioner has apparently not focused on the issue, Part A premium payments made by voluntary enrollees are presumably to be taken into account as amounts paid for insurance covering medical care, and allowed in computing the medical expense deduction under Section 213(a) and (c)(1)(C) of the Code.

CONCLUSION

The Tax Court correctly determined that hospital expenses paid with the proceeds of Part A Hospital Insurance are not part of an individual's "support" in determining the dependency exemption. That conclusion is required by the essential insurance nature of Part A Hospital Insurance. As with private hospital insurance and Part B Supplementary Medical Insurance, the appropriate support item is instead the individual's periodic contribution to the insurance fund, whether by premium payments or by payroll taxes.

The decision of the Tax Court should be affirmed.

Respectfully submitted,

MICHAEL H. SIMONSON
Attorney for Appellees
350 Park Avenue
New York, New York 10022
(212) 483-9000

AFFIDAVIT OF SERVICE BY MAIL

STATE OF NEW YORK)
: ss.:
COUNTY OF NEW YORK)

MARIE MULHALL , being duly sworn, deposes and says:

I am over the age of eighteen (18) years and am not a party to this action.

On the 28th day of July , 1976, I served a copy of the annexed paper upon

Scott P. Crampton
Assistant Attorney General
Tax Division
Department of Justice
Washington, D.C. 20530

by depositing a true copy of the same in a properly addressed postpaid wrapper in a regularly maintained official depository under the exclusive care and custody of the United States Post Office Department located in the City, County and State of New York.

Marie Mulhall

Sworn to before me this
28th day of July , 1976.

Joseph G. DeRespino

JOSEPH G. DE RESPINO
NOTARY PUBLIC, STATE OF NEW YORK
No. 41-4607926
Qualified in Queens County
Certificate Filed in New York County
Commission Expires March 30, 1977